IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
LUBBOCK DIVISION

IN RE:	§	
	§	
CORNWALL PERSONAL INSURANCE AGENCY, INC.,	§	CASE NO. 02-50463-RLJ-11
	§	
	§	
DEBTOR	§	

MEMORANDUM OPINION

Before the court are two issues: (1) whether Cornwall Personal Insurance Agency's ("Cornwall's") Chapter 11 First Amended Plan ("Plan"), as revised at the confirmation hearing, should be confirmed under section 1129(b) of the Bankruptcy Code, and (2) whether Cornwall's motion to assume its unexpired commercial lease should be approved. William David Brenholtz ("Brenholtz"), a judgment creditor, objects to confirmation and to Cornwall's assumption of its lease.

This court has jurisdiction of this matter under 28 U.S.C. §§ 1334 and 157. This is a core proceeding pursuant to 28 U.S.C. § 157(b). This Memorandum Opinion contains the court's findings of fact and conclusions of law. FED. R. BANKR. P. 7052.

Court's Ruling

The court denies confirmation as Cornwall failed to meet its burden of establishing that the Plan's treatment of Brenholtz's claim satisfies the fair and equitable standard of section 1129(b) of the Code. The fair and equitable standard was not specifically raised by the parties at the confirmation hearing. The court addresses the issues presented and concludes that Cornwall's Plan, apart from the fair and equitable standard, otherwise meets the requirements for confirmation. Cornwall is therefore allowed 20 days from entry of the order denying

confirmation to file a modified plan. The court approves Cornwall's motion seeking assumption of the commercial lease.

I. Facts and Issues

Cornwall filed this Chapter 11 case on April 12, 2002. The event that forced Cornwall to seek bankruptcy protection was a state court judgment obtained by Brenholtz in the 364th District Court of Lubbock County, against Cornwall, Ron Hettler, who is Cornwall's sole shareholder, and Robin Hettler, Ron Hettler's wife. The judgment, which includes punitive damages, is for breach of contract, tortious interference with business relationships, conversion, and fraud – all arising from the former business relationship between Brenholtz and Cornwall and the Hettlers. While there is some disagreement about the final amount of the judgment, Brenholtz's proof of claim reflects a judgment against Cornwall of $495,652.22, on which Robin Hettler and Ron Hettler are, in part, jointly and severally liable. Shortly after the state court rendered its judgment, Brenholtz proceeded to attempt to collect from Cornwall and the Hettlers. Unable to post a supersedeas bond pending appeal, Cornwall filed this Chapter 11 case, and the Hettlers filed a separate Chapter 11 case.

Cornwall and the Hettlers have appealed the state court judgment. The parties believe the appeal will be heard and decided within one year. This court has lifted the stay and approved employment of special counsel to prosecute the appeal. Cornwall believes it has a good chance of reversing the judgment in favor of Brenholtz, or, at least, of reducing the judgment. Of additional importance is Cornwall's contention that its insurer, Travelers Lloyd Insurance Company ("Travelers"), improperly denied coverage for Brenholtz's claim and thus failed to

provide a defense to the claim.[1] Cornwall and the Hettlers have therefore initiated an action against Travelers in the 72nd District Court of Lubbock County, to recover for breach of contract and breach of duty for Traveler's alleged failure to provide a defense and coverage. The court has lifted the stay and approved the employment of special counsel to enable Cornwall to prosecute this action.

Brenholtz's claim is unsecured. The Plan places Brenholtz's claim in Class 6, while it places all other unsecured claims from non-insiders in Class 4. The Plan proposes to pay Brenholtz and the Class 4 unsecured creditors in full, albeit on a deferred basis. Ron Hettler retains his interest in Cornwall. Specifically, the Plan proposes to pay the Class 4 claimants over a twenty-four month period, with monthly payments of $870 each. This is a mistake, as $870 over twenty-four months amounts to double the total amount of allowed claims in Class 4.[2] The court construes the plan as proposing the $870 per month payment to Class 4 until such class is paid in full, approximately twelve months after the effective date of the Plan. Class 4 does not

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[1]In a hearing held before this court on July 24, 2002, counsel for Brenholtz stated, "I was the attorney of record in the underlying case and recognizing what the coverages were and available under that policy, we made a decision to plead the case so there would be no coverage." Debtor's Ex. E.

[2]With respect to Class 4, Cornwall's First Amended Combined Plan and Disclosure Statement lists the total amount of Class 4 at $26,487.54, and provides that "[a]ll allowed claims will be paid 1/24th of claim each month over 24 months at 0.0% interest." Cornwall's Revised Plan Treatment, submitted at the confirmation hearing, lists the total amount of Class 4 at $10,500, and provides that "[a]ll allowed claims will be paid 1/24th of claim each month over 24 months at 0.0% interest. with [sic] monthly payments of approximately $870."

The revised treatment is erroneous, because, at $870 per month, it would take approximately one year to pay off Class 4, as opposed to the two years stated by Cornwall. Which is correct: is Class 4 to be paid over two years, or over one year at $870 per month? More than likely, the $870 per month figure is correct. Significantly, $870 per month over two years would not amount to the $26,487.54 total of Class 4 in the amended Plan. Thus, the $870 per month figure was added after the amended Plan, and appeared for the first time in the revised treatment. This leads to the conclusion that $870 per month is correct, while the two year language was left over inadvertently from the language of the amended Plan. Additionally, the mistake in the revised treatment, where the period remains followed by a lower case 'with,' suggests that the clause beginning 'with' was added in haste, without regard to the contradiction the addition of such clause would create.

receive interest.

The Plan provides that Brenholtz's claim will accrue interest at 6% per annum and calls for an initial $2,000 per month payment against Brenholtz's claim. These payments are placed in an escrow account until the appeal is resolved; if resolved in favor of Brenholtz, Brenholtz will then collect the funds in escrow, and Cornwall will begin making payments directly to Brenholtz. The $2,000 per month payment will increase as other classes are retired, to a maximum of $6,000 per month some sixty months after confirmation. Payments will never exceed $6,000, and will continue until Brenholtz's claim, including interest, is paid in full. The Plan also proposes to pay Brenholtz any recovery that Cornwall may be awarded as a result of its suit against Travelers. In the absence of any such recovery, and assuming that Cornwall is unsuccessful on its appeal, Cornwall estimates that it may take up to twelve and one half years to pay Brenholtz's claim in its entirety, including payments, if any, that the Hettlers will make to Brenholtz under their separate Chapter 11 plan.

Cornwall relies on the cram down provision of section 1129(b) for confirmation of the Plan. Brenholtz has voted against the Plan. Class 4, which constitutes the only impaired class of non-insider claims, voted to accept the Plan. Thus Class 4 is the only impaired consenting class.

Brenholtz objects to confirmation on several grounds. Chief among these grounds is Brenholtz's argument that the Plan impermissibly classifies his claim separate from the claims of other unsecured creditors. Specifically, Brenholtz argues that Cornwall separately classified his claim for the sole purpose of gerrymandering an affirmative vote of an impaired class. Additionally, Brenholtz argues that the Plan unfairly discriminates against his claim. Namely, Brenholtz complains that he, unlike all other unsecured creditors, will receive nothing under the

Plan until a final resolution of Cornwall's appeal; that all other unsecured creditors will be paid in full well before Brenholtz; and that the Plan fails to commit the full range of Cornwall's available resources to pay claims. Finally, Brenholtz argues that Cornwall has not proposed the Plan in good faith.

Brenholtz objects to Cornwall's motion to assume its unexpired commercial lease on the grounds that such assumption is not in the best interests of the estate or its creditors because Cornwall pays more for the lease than it needs in order to carry on its operations. Furthermore, Brenholtz points to the fact that the lessor, Ron Hettler, is an insider of Cornwall, and argues that the contemplated assumption benefits Hettler personally instead of Cornwall's estate.

II. Discussion

The court will first discuss the classification issue, then the unfair discrimination and lack of good faith claims. Though not specifically argued by the parties, the court will address the question whether the Debtor's treatment of Brenholtz's claim satisfies the fair and equitable standard under section 1129(b) of the Code. Finally, the court will address Cornwall's motion seeking to assume its lease. Except where specifically discussed, the court will not address the remaining confirmation requirements under section 1129(a) of the Code as there is no dispute that Cornwall has satisfied such unaddressed requirements.

A. Separate Classification of Brenholtz's Claim

Section 1122 provides that "a plan may place a claim or interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class." 11 U.S.C. § 1122(a) (2002). By its express language, section 1122 provides that dissimilar claims cannot be included in the same class; it does not mandate that all similar claims be placed in the

same class. *See In re Dow Corning Corp.*, 280 F.3d 648, 661 (6th Cir. 2002). Similar claims may be classified separately in appropriate instances. *See id.* Nevertheless, "many courts, including five circuit courts of appeal, while recognizing that § 1122 does not explicitly forbid a plan proponent from placing similar claims in separate classes, have imposed significant limits on the ability of a plan proponent to do so." *In re SM 104 Ltd.*, 160 B.R. 202, 216 (Bankr. S.D. Fla. 1993). Thus, under both sections 1122 and 1129(b), "'substantially similar claims,' those which share common priority and rights against the debtor's estate, should be placed in the same class." *Phoenix Mut. Life Ins. Co. v. Greystone III Joint Venture (In the Matter of Greystone III Joint Venture)*, 995 F.2d 1274, 1278 (5th Cir. 1991).

The plan proponent bears the burden of establishing that its plan conforms with all applicable confirmation standards, which the plan proponent may meet by a preponderance of the evidence. *See Heartland Fed. Sav. & Loan Ass'n v. Briscoe Enters. Ltd. (In the Matter of Briscoe Enters. Ltd.)*, 994 F.2d 1160, 1165 (5th Cir. 1993). This includes the plan's classification of, and discrimination between, similar claims. *See id.* In this regard, the debtor has considerable, albeit not unlimited, discretion in classifying creditors. *See In the Matter of Wabash Valley Power Ass'n Inc.*, 72 F.3d 1305, 1321 (7th Cir. 1995); *In the Matter of Greystone III Joint Venture*, 995 F.2d at 1279. The court likewise has substantial discretion in confirming a plan that separately classifies similar claims. *See In re Dow Corning Corp.*, 280 F.3d at 661; *Steelcase Inc. v. Johnston (In re Johnston)*, 21 F.3d 323, 327 (9th Cir. 1994). Equitable considerations play little, if any role, in the court's decision on classification. *See Aetna Cas. & Sur. Co. v. Clerk, U.S. Bankr. Court N.Y.N.Y (In re Chateaugay Corp.)*, 89 F.3d 942, 947 (2d Cir. 1996) ("the Bankruptcy Code and not the law of equity governs the dispute" concerning

classification).

"The power to separately classify creditors is subject to a limitation that some reasonable grounds must exist in order to authorize the proposed classification scheme . . . ." *In re General Homes Corp. FGMC Inc.*, 134 B.R. 853, 863 (Bankr. S.D. Tex. 1991). *Accord In re Apex Oil Co.*, 118 B.R. 683, 696 (Bankr. E.D. Mo. 1990) ("If the Debtors had separately classified an objecting unsecured creditor, the Court would be required to find some 'unique' interest to justify the separate classification"). Such a reasonable ground generally falls within one or more of three categories: (1) legitimate business reason; (2) disparities between the legal rights of holders of different claims; or (3) claimants have sufficiently different interests in the plan. *See, e.g., In the Matter of Wabash Valley Power Ass'n Inc.*, 72 F.3d at 1321.

One instance, however, where separate classification of similar claims is clearly inappropriate under both sections 1122 and 1129(b) is when similar claims are separately classified for the purpose of gerrymandering an affirmative vote on the plan of reorganization. *See In the Matter of Greystone III Joint Venture*, 995 F.2d at 1279 ("thou shalt not classify similar claims differently in order to gerrymander an affirmative vote on a reorganization plan"). The court should not approve the separate classification if the plan proponent's proffered reasons for separate classification "simply mask the intent to gerrymander the voting process." *Id.* Thus, because Cornwall's Plan is based on cram down, and because the only consenting impaired class would not have consented had Brenholtz been a part of such class, if the court can find no reasonable ground to warrant separate classification, the only conclusion left is that Cornwall separately classified Brenholtz's claim for the purpose of gerrymandering an affirmative vote of an impaired class. If this is the case, the court should deny confirmation of Cornwall's Plan.

See id.

Good Business Reason

A debtor may separately classify similar claims when separate classification is supported by a legitimate business reason. *See Bakarat v. Life Ins. Co. of Va. (In re Bakarat)*, 99 F.3d 1520, 1526 (9th Cir. 1996); *In re Chateaugay Corp.*, 89 F.3d at 949. The Fifth Circuit has recognized this principle, except that it phrases the inquiry in terms of 'good business reason' for the separate classification. *See In the Matter of Briscoe Enters. Ltd.*, 994 F.2d at 1167. The debtor bears the burden of establishing such good business reason, which the debtor must establish by credible proof. *See In re Bakarat* 99 F.3d at 1526; *In re Chateaugay Corp.*, 89 F.3d at 949; *In the Matter of Greystone III Joint Venture*, 995 F.2d at 1281. If the debtor advances a business reason for the separate classification, yet fails to substantiate such business reason, separate classification will not be allowed. *See In the Matter of Greystone III Joint Venture*, 995 F.2d at 1281 (reversing bankruptcy court's finding that good business reasons for separate classification existed, because such decision was unsupported by the record; debtor failed to prove existence of good business reasons). Whether the debtor establishes a good business reason for separate classification is a question of fact. *See In the Matter of Briscoe Enters. Ltd.*, 994 F.2d at 1167.

For example, the debtor's separate classification of trade creditors from other unsecured creditors may be permitted if the debtor's business relies on the continued cooperation and goodwill of such trade creditors, and such cooperation and goodwill may be obtained only through separate (and presumably preferential) classification and treatment. *See, e.g., In the Matter of Greate Bay Hotel & Casino Inc.*, 251 B.R. 213, 223-24 (Bankr. D.N.J. 2000). In

Briscoe, the Fifth Circuit permitted the debtor, a real estate developer, to separately classify the City of Fort Worth's unsecured claim from other unsecured claims. *See In the Matter of Briscoe Enters. Ltd.*, 994 F.2d at 1167. In addition to being a creditor, the city paid rental assistance to the debtor on behalf of low income tenants. *See id.* The Fifth Circuit stated:

> Not only does [City] have non-creditor interests relating to its urban housing program, but it contributes $20,000 a month in rental assistance. [Objecting Creditor] argues that the plan is not feasible because there is no assurance of continued rental assistance from the city. This argument suggests that the relationship with the city is essential to the continued operation of this housing complex. Its continuing contributions and interests make it distinct from [Objecting Creditor] and the trade creditors. We emphasize the narrowness of this holding. In many bankruptcies, the proffered reasons as in *Greystone* will be insufficient to warrant separate classification. Here it seems justified.

Id. Thus, the Fifth Circuit permitted separate classification of unsecured claims on the basis of, among other reasons, a good business reason; namely, the debtor's need to continue good relations with the city in order to receive continuing rental assistance. *See id.*

Different Legal Rights

A plan may separately classify claims when disparities exist between the legal rights of holders of different claims. *See In the Matter of Wabash Valley Power Ass'n Inc.*, 72 F.3d at 1321; *In the Matter of Greystone III Joint Venture,* 995 F.2d at 1279; *In re General Homes Corp. FGMC Inc.*, 134 B.R. at 863. While there appears to be some dispute among the circuits as to whether the resolution of this issue is a question of fact or of law, the Fifth Circuit has stated that "[w]hether a deficiency claim is legally similar to an unsecured trade claim turns not on fact findings but on their legal characteristics. This is an issue of law, freely reviewable on appeal." *In the Matter of Greystone III Joint Venture*, 995 F.2d at 1279 n. 5. *But see Steelcase Inc v. Johnston (In re Johnston)*, 21 F.3d 323, 327 (9th Cir. 1994) (holding that whether claims

are substantially similar is a question of fact). Thus it appears that whether or not separate classification is justified based on legal differences between claims is a question of law, although "[s]ubsidiary fact findings [] may be entitled to the deference of the clearly erroneous test." *In the Matter of Greystone III Joint Venture*, 995 F.2d at 1279 n. 5.

Secured creditors that hold liens against different properties owned by the debtor have different legal rights. *See In re General Homes Corp. FGMC Inc.*, 134 B.R. at 863-64. Likewise, priority claimants may be placed in separate classes based on their differing priorities, because a higher priority claimant has a different legal right to be paid than does a lower priority claimant, who may receive nothing if the higher priority claimant is not paid. *See id.* Contingent claims are legally different from fixed claims, and the holders of contingent claims have different legal rights against the estate. *See, e.g., In re Bakarat*, 99 F.3d at 1527; *In re Dow Corning Corp.*, 244 B.R. 634, 651 (Bankr. E.D. Mich. 1999).

With respect to unsecured creditors, such creditors may be placed into different classes even though they are all unsecured, based, for example, on the debtor's subordination agreements with such creditors, because creditors with subordinated claims have a different right to payment than those with 'senior' debt. *See In re General Homes Corp. FGMC Inc.*, 134 B.R. at 863-64. However, the manner by which claims achieved their status "does not alter their current legal character and thus does not warrant separate classification." *Lumber Exchange Bldg. Ltd. P'ship v. Mutual Life Ins. Co. of N.Y. (In re Lumber Exchange Bldg. Ltd. P'ship)*, 968 F.2d 647, 649 (8th Cir. 1992) (holding that creditor's section 1111(b) deficiency claim may not be separately classified from unsecured trade creditors because, while such claims arose differently, they were all general unsecured claims). *Accord John Hancock Mut. Life Ins. Co. v. Route 37 Bus. Part*

Assocs., 987 F.2d 154, 160-61 (3d Cir. 1993).

Different Interests in Plan

Legally similar claimants may be classified separately if they have sufficiently different interests in the plan. *See In the Matter of Wabash Valley Power Ass'n Inc.*, 72 F.3d at 1321; *Teamsters Nat'l Freight Indus. Negotiating Comm. v. U.S. Truck Co. Inc. (In re U.S. Truck Co. Inc.)*, 800 F.2d 581, 587 (6th Cir. 1986). This basis for separate classification is akin to the good business reason basis, except that it analyzes the situation from the creditor's viewpoint. *See In re EBP Inc.*, 172 B.R. 241, 244 (Bankr. N.D. Ohio 1994). In other words, just as a debtor may have a legitimate business reason for separately classifying certain unsecured claimants, so too may the unique interests or circumstance of a creditor justify separate classification. *See id.* ("the principal basis for allowing the separate classification was that the two separate classes of unsecured creditors had a different stake in the future viability of the reorganized debtor and the unsecured trade creditors also possessed alternative means at their disposal for protecting their claims"). Such a creditor may have different interests in the plan than do other unsecured creditors. *See e.g., In the Matter of Briscoe Enters. Ltd.*, 994 F.2d at 1167; *In re U.S. Truck Co. Inc.*, 800 F.2d at 587 ("The Teamsters Committee may choose to reject the plan not because the plan is less than optimal to it as a creditor, but because the Teamsters Committee has a noncreditor interest – e.g., rejection will benefit its members in the ongoing employment relationship").

Thus, for example, the Seventh Circuit permitted separate classification of unsecured claims where the creditor separately classified had entered into a settlement with the debtor, the effectiveness of which was contingent upon confirmation of the debtor's plan. *See In the Matter*

of Wabash Valley Power Ass'n Inc., 72 F.3d at 1321. Additionally, the creditor had ongoing business relations with the debtor. *See id.* The Seventh Circuit stated, "[b]ecause the confirmation of this Plan affects [Creditor's] interests both with respect to its settlement of other litigation between it and [Debtor] and with respect to its ongoing business relationship with [Debtor], its stake in [Debtor's] reorganization differs significantly enough from that of the other unsecured creditors to warrant the separate classification of its claims." *Id.* Likewise, in *Briscoe*, the Fifth Circuit permitted separate classification for the apparent reason that the city's interests in the successful reorganization of the debtor were sufficiently different from the interests of other unsecured creditors, as the city depended on the debtor to provide housing to low income tenants and thus had interests other than mere repayment to protect. *In the Matter of Briscoe Enters. Ltd.*, 994 F.2d at 1167. The circuit stated that the city "is distinct from other creditors including [Objecting Creditor]. Not only does it have non-creditor interests, but it contributes $20,000 a month in rental assistance . . . . Its continuing contributions and interests make it distinct from" other unsecured creditors. *Id.*

Application to Brenholtz's Claim

With respect to the separate classification of Brenholtz's claim, Cornwall fails to meet the good business reason for separate classification – at least as such basis has been typically articulated by the courts. Cornwall does not rely on continued business dealings with Brenholtz. *See, e.g., In the Matter of Greate Bay Hotel & Casino Inc.*, 251 B.R. 213, 223-24 (Bankr. D.N.J. 2000) (permitting separate classification of trade creditors' claims, because the debtor's business relied on the continued cooperation and goodwill of such trade creditors). In addition, Cornwall offered no argument or evidence regarding ongoing business relations with its other unsecured

creditors (the Class 4 claimants), or the need to treat such unsecured creditors in a manner different from Brenholtz in order to insure ongoing and favorable business relations. *See, e.g., Bakarat v. Life Ins. Co. of Va. (In re Bakarat)*, 99 F.3d 1520, 1528 (9th Cir. 1996) (disallowing separate classification of trade creditors because "thousands of companies are available to provide the services of the trade creditors, thus none of the trade creditors were essential to Debtor's continued maintenance of the apartment building").

An argument may be made that Cornwall justifies separate classification of Brenholtz's claim on the basis that Brenholtz has different interests in the Plan as compared with other unsecured creditors. Brenholtz may be considered Cornwall's competition and, as such, has little interest in seeing Cornwall succeed under a reorganization plan. If Cornwall fails, Brenholtz's claim would share in Cornwall's book of business, which consists of insurance contracts.

Brenholtz's desire to see Cornwall liquidate does not, however, justify separate classification. The court believes that Brenholtz's real, overriding goal is to maximize payment on his claim – the same goal of most unsecured creditors in any case.

The best justification for separate classification of Brenholtz's claim is that Brenholtz has different legal rights regarding his claim than do other unsecured creditors. There is support for the proposition that a claim based on a judgment is different from other unsecured claims. *See Steelcase Inc. v. Johnston (In re Johnston)*, 21 F.3d 323, 327 (9th Cir. 1994); *In re EBP Inc.*, 172 B.R. at 244; *In the Matter of Rochem Ltd.*, 58 B.R. 641, 642-43 (Bankr. D.N.J. 1985).[3] However,

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[3]In *In re EBP Inc.*, for example, the court permitted the debtor to separately classify a judgment creditor's claim from the unsecured claims of trade creditors. *See id.* The court permitted this classification, holding that the judgment creditor's claim

> is a non-recurring judicial event, providing no continuing benefit to the Debtor's estate, whereas the

there is also authority for the opposite conclusion. *See In re Salem Suede Inc.*, 219 B.R. 922, 933 (Bankr. D. Mass. 1998).

For purposes of this case, the court returns to the premise that the manner by which creditors achieve their status "does not alter their current legal character and thus does not warrant separate classification." *Lumber Exchange Bldg. Ltd. P'ship v. Mutual Life Ins. Co. of N.Y. (In re Lumber Exchange Bldg. Ltd. P'ship)*, 968 F.2d 647, 649 (8th Cir. 1992). *Accord John Hancock Mut. Life Ins. Co. v. Route 37 Bus. Part Assocs.*, 987 F.2d 154, 160-61 (3d Cir. 1993). In one sense, Brenholtz has the same legal rights as other unsecured creditors, because Brenholtz himself is an unsecured creditor, and unsecured creditors have the same rights under the Code. *See In re Salem Suede Inc.*, 219 B.R. at 933 ("Although the Judgment Creditors' claims against the Debtors arose in a different fashion from other unsecured and trade debt, their unsecured claims are of a legal character indistinguishable from that debt"). Thus, the mere fact that Brenholtz's claim arose as the result of a judgment, rather than under contract or other means, is not, in this court's view, sufficient ground, taken alone, to warrant separate classification of Brenholtz's claim.

But, Brenholtz's claim differs from other unsecured claims in two important respects: (1) Brenholtz's claim is subject to a reversal on appeal; and, (2) Brenholtz's claim is based, in part,

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> trade creditors, while also unsecured, do provide a potential continuing benefit which will sustain the Debtor's business if confirmation is achieved. The converse is true from the Debtor's position. Also of significant note is the fact that the [judgment] claim is the single largest unsecured claim, representing approximately 70% of all the unsecured debt. This comparison provides the requisite dissimilarity to warrant a separate classification of the aforesaid claimants pursuant to § 1122(a) of the Code.

In re EBP Inc., 172 B.R. 241, 244 (Bankr. N.D. Ohio 1994).

on joint and several liability of Cornwall, Robin Hettler, and Ron Hettler. The question is whether one or both of these differences create sufficient distinctions between the legal rights of Brenholtz and those of other unsecured creditors to warrant separate classification.

"Whether the issue on appeal is denial of separate classification or approval of separate classification, the question resolved by the bankruptcy court is the same: are the claims substantially similar? To resolve that question, bankruptcy court judges must evaluate the nature of each claim, i.e., the kind, species, or character of each category of claims." *In re Johnston*, 21 F.3d at 327. Courts have permitted separate classification of similar claims when one such claim is contingent, because this contingency evidences different legal rights between claimants. *See In re Bakarat*, 99 F.3d at 1527 (affirming separate classification on basis that contingent and unliquidated claims were legally different from other unsecured claims); *In re Dow Corning Corp.*, 244 B.R. 634, 651 (Bankr. E.D. Mich. 1999), *aff'd in part*, 280 F.3d 648 (6th Cir. 2002) (affirming separate classification).

Generally, a claim based on a final state court judgment – even where the courts of the state do not afford such judgment res judicata effect – is neither contingent nor unliquidated despite the possibility that such judgment may be reversed on appeal. *See Audre Inc. v. Casey (In re Audre Inc.)*, 216 B.R. 19, 30 (B.A.P. 9th Cir. 1997); *In re Mitchell*, 255 B.R. 345, 359 (Bankr. D. Mass. 2000); *In re Wilkinson*, 196 B.R. 311, 314 n.2 (Bankr. E.D. Va. 1996) ("Since the debt had been reduced to judgment, to characterize it as 'unliquidated' was plainly improper"). In other words, the possibility of reversal on appeal does not make a claim contingent or unliquidated under the Bankruptcy Code's definitions of such terms. *See id.*

Although Brenholtz's claim is not contingent under the Code's definition as the

conditions precedent to his claim have been satisfied, Brenholtz's claim is contingent on a condition subsequent – the possibility of reversal on appeal. The court considers the practical differences in the legal rights of Brenholtz compared to those of other unsecured creditors. *See In re Johnston*, 21 F.3d at 327 (noting that the legal nature of a claim is not dependant only on technical definitions, but on ordinary and practical differences); *In re National/Northway Ltd. P'ship*, 279 B.R. 17, 27-28 (Bankr. D. Mass. 2002). In this regard, the court cannot ignore the possibility, however remote, that Brenholtz's claim might be reversed or reduced on appeal. No other unsecured claim faces this possibility. Similarly, Brenholtz's claim is based, in part, on joint and several liability of Cornwall and the Hettlers. Cornwall's ultimate liability to Brenholtz depends on whether the Hettlers make payments on the joint and several debt. No other unsecured claim arises from joint and several liability, and no other unsecured claim is therefore subject to a variable amount of debt depending on the amount of payment from other parties.

Additionally, of all the unsecured creditors, Brenholtz alone is involved in ongoing litigation with Cornwall. As explained by the Ninth Circuit:

> Steelcase must also concede that it, unlike all other unsecured creditors, is embroiled in litigation with Johnston, and that its claim thus may be offset or exceeded by Johnston's own claim against Steelcase . . . . Under these circumstances, the bankruptcy court was not clearly erroneous in concluding that Steelcase's claim is distinguishable from Class 19, Class 20, and Class 22 claims . . . . Steelcase's separate classification under the Johnston plan does not violate § 1122(a) because the legal character of its claim is not substantially similar to the other claims or interests of such classes. This is so because, as we have already stated, the bankruptcy court did not commit clear error in finding that Steelcase was the only unsecured creditor whose claim is currently being litigated.

In re Johnston, 21 F.3d at 328 (internal quotations and citations omitted).

Real differences exist between Brenholtz and other unsecured creditors: (1) Brenholtz's claim is subject to a reversal on appeal; (2) Brenholtz's claim is partially based on joint and several liability; and (3) Brenholtz is engaged in continuing litigation with Cornwall. *See In re Johnston*, 21 F.3d at 327; *In re National/Northway Ltd. P'ship*, 279 B.R. at 27-28. These differences justify separate classification of Brenholtz's claim. *See id. See also In re Dow Corning Corp.*, 211 B.R. at 565 n.18; *In re EBP Inc.*, 172 B.R. at 244; *In the Matter of Rochem Ltd.*, 58 B.R. 641, 642-43 (Bankr. D.N.J. 1985). Cornwall's intent in separately classifying Brenholtz's claim was not for the sole purpose of gerrymandering an affirmative vote from an impaired class. *See Phoenix Mut. Life Ins. Co. v. Greystone III Joint Venture (In the Matter of Greystone III Joint Venture)*, 995 F.2d 1274, 1279 (5th Cir. 1991).

B. Unfair Discrimination

Apart from the classification issue is the issue of whether Cornwall's Plan unfairly discriminates against Brenholtz's claim. Section 1129(b)(1) provides that a court may confirm a plan under cram down only if "the plan does not discriminate unfairly . . . with respect to each class of claims or interests that is impaired under, and has not accepted, the plan." 11 U.S.C. § 1129(b)(1) (2002). Brenholtz argues that Cornwall's Plan violates this requirement for the apparent reason that "Debtor does not begin paying [Brenholtz's] claim until a final resolution of the underlying case of Brenholtz or the final resolution of other lawsuits filed by Debtor." Objection of David Brenholtz to Debtor's First Amended Combined Plan and Disclosure Statement ¶ 3. Brenholtz additionally objects because, under the Plan, Class 4 claims will be paid off in approximately one year, while Brenholtz's claim may take up to twelve and one half years to pay off.

When relying on cram down, the plan proponent must satisfy the requirement that its plan not discriminate unfairly. *See, e.g., Oxford Life Ins. Co. v. Tucson Self-Storage Inc. (In re Tucson Self-Storage Inc.)*, 166 B.R. 892, 898 (B.A.P. 9th Cir. 1994). "Unfair discrimination is best viewed as a horizontal limit on nonconsensual confirmation . . . . Just as the fair and equitable requirement regulates priority among classes of creditors having higher and lower priorities, creating inter-priority fairness, so the unfair discrimination provision promotes intra-priority fairness, assuring equitable treatment among creditors who have the same level of priority." *In re Sentry Operating Co. of Tex. Inc.*, 264 B.R. 850, 863 (Bankr. S.D. Tex. 2001), *quoting* Bruce A. Markell, *A New Perspective on Unfair Discrimination in Chapter 11*, 72 AM. BANKR. L. J. 227, 227 (1998). Thus, although similar claims may be separately classified, similar claims within the same priority must nevertheless be accorded treatment which does not discriminate unfairly between such claims. *See In re Tucson Self-Storage Inc.*, 166 B.R. at 898. "[T]he Bankruptcy Code is premised on the rule of equality of treatment." *In re Sentry Operating Co. of Tex. Inc.*, 264 B.R. at 863.

For example, a Chapter 11 plan discriminates against a class when it proposes to pay such class a lower percentage than a class of similar claims. *See, e.g., In re Salem Suede Inc.*, 219 B.R. 922, 933-34 (Bankr. D. Mass. 1998); *Creekstone Apartments Assocs. L.P. v. Resolution Trust Corp. (In re Creekstone Apartments Assocs. L.P.)*, 168 B.R. 353, 641-42 (Bankr. M.D. Tenn. 1994). Similarly, a plan discriminates against a class when it proposes to pay such class over a period of years without interest, while paying a similar class in full upon the effective date of the plan. *See, e.g., In re Cranberry Hill Assocs. Ltd. P'ship*, 150 B.R. 289, 290-91 (Bankr. D. Mass. 1993). Likewise, a plan discriminates against a class by proposing to pay such class a

lump sum payment at some point in the future, while providing periodic payments to a similar class in the meantime. *See, e.g., In re McNichols*, 254 B.R. 422, 428-29 (Bankr. N.D. Ill. 2000). Thus a difference in the percentage of recovery or in the timing of recovery, between similar claims or classes, may constitute discrimination.

Discrimination is permissible; unfair discrimination is not. *See In re Sentry Operating Co. of Tex. Inc.*, 264 B.R. at 863; *In re 11,111 Inc.*, 117 B.R. 471, 478 (Bankr. D. Minn. 1990). The Code does not define the concept of unfair discrimination. *See In the Matter of Greate Hotel & Casino Inc.*, 251 B.R. 213, 228 (Bankr. D.N.J. 2000). The court should consider the totality of the circumstances in determining whether a proposed discrimination is unfair. *See In re Freymiller Trucking Inc.*, 190 B.R. 913, 916 (Bankr. W.D. Okla. 1996). Courts have advanced numerous factors to consider when determining whether discrimination is unfair. The recently emerging trend, which synthesizes to a large extent the prior case law, is to create a rebuttable presumption of unfair discrimination "when there is: (1) a dissenting class; (2) another class of the same priority; and (3) a difference in the plan's treatment of the two classes that results in either (a) a materially lower percentage recovery for the dissenting class (measured in terms of the net present value of all payments), or (b) regardless of percentage recovery, an allocation under the plan of materially greater risk to the dissenting class in connection with its proposed distribution." *In the Matter of Greate Hotel & Casino Inc.*, 251 B.R. at 228-29. *Accord In the Matter of Genesis Health Ventures Inc.*, 266 B.R. 591, 611 (Bankr. D. Del. 2001); *In re Sentry Operating Co. of Tex. Inc.*, 264 B.R. at 863-64; *In re Dow Corning Corp.*, 244 B.R. 696, 702 (Bankr. E.D. Mich. 1999).

In the case at bar, the first two elements are met: Brenholtz has voted against the Plan

and Brenholtz's claim is of the same priority as Class 4. With respect to the third element, Cornwall's treatment of Brenholtz's claim differs from its treatment of Class 4 claims in two respects: first, Cornwall will pay $2,000 per month into an escrow account, which Brenholtz may collect when and if Cornwall is unsuccessful on its appeal, while Class 4 claims are to be paid directly to claimants immediately upon confirmation; second, Cornwall's Plan proposes to pay Class 4 claims in approximately one year, while Brenholtz's claim may take up to twelve and one half years to pay in full.

Cornwall's proposed payments into an escrow account until such time as Brenholtz succeeds on the appeal is not unfairly discriminatory. Cornwall's Plan proposes to pay both Brenholtz and the Class 4 claims in full.[4] Additionally, as the Brenholtz payments will be placed in escrow and his claim will bear interest, risk of nonpayment is no greater for Brenholtz than it is for the Class 4 creditors. Brenholtz's only risk is that he may lose on appeal, which is a risk he faces regardless. Escrowing initial payments to Brenholtz pending appeal does not, therefore, trigger the rebuttable presumption of unfair discrimination. *See In re Sentry Operating Co. of Tex. Inc.*, 264 B.R. at 863-64.

The Class 4 claims will be paid in full many years before Brenholtz's claim is paid. Brenholtz faces greater risk because there is no guarantee that Cornwall will be able to make its payments several years into the future – at which time Class 4 claims will have been paid in full.

[4]By stating that Brenholtz and the Class 4 claimants are paid "in full" the court is simply referring to payment *over time* of the entire amount of such claims. The court is not stating that such claims are paid their present value. *See* discussion *infra* Part II.D.

See, e.g., In re Cranberry Hill Assocs. Ltd. P'ship, 150 B.R. at 290-91.[5] This arguably gives rise to the rebuttable presumption of unfair discrimination. *See In the Matter of Greate Hotel & Casino Inc.*, 251 B.R. at 228-29.

The plan proponent may rebut the presumption of unfair discrimination, or otherwise demonstrate that the plan – while discriminatory – does not discriminate unfairly. Courts generally look to four factors in deciding whether the proposed discrimination is unfair:

(1) does the discriminatory treatment have a reasonable basis;

(2) could the debtor carry out a plan without the discrimination;

(3) is the plan, and, in turn, the discriminatory treatment proposed in good faith; and

(4) the treatment of the discriminated class.

See Liberty Nat'l Enters. v. Ambanc La Mesa Ltd. P'ship (In re Ambanc La Mesa Ltd. P'ship), 115 F.3d 650, 656 (9th Cir. 1997); *In the Matter of Genesis Health Ventures Inc.*, 266 B.R. 591, 611 (Bankr. D. Del. 2001); *In re Aztec Co.*, 107 B.R. 585, 590 (Bankr. M.D. Tenn. 1989); *In the Matter of Rochem Ltd.*, 58 B.R. 641, 643 (Bankr. D.N.J. 1985). Additionally, many courts consider the degree of the discrimination, i.e. whether "the degree of discrimination is in direct proportion to its rationale." *In re Buttonwood Partners Ltd.*, 111 B.R. 57, 63 (Bankr. S.D.N.Y. 1990). *Accord In re HRC Joint Venture*, 187 B.R. 202, 211 (Bankr. S.D. Ohio 1995).

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[5]The court in *Cranberry Hill* stated:

> The Court agrees that the plan discriminates unfairly on its face. The Class Six claimants would receive the full amounts of their claims on the effective date of the plan out of funds on hand at confirmation; their payments are virtually immediate and risk free. The same cannot be said for Prudential. Even if payment of Prudential's claim were certain, the bulk of the claim would not be paid for nine years . . . payment in full in nine years is far from certain . . . and its claim will be subject to much higher risk of nonpayment.

In re Cranberry Hill Assocs. Ltd. P'ship, 150 B.R. at 290-91.

The question, then, is whether payment of the Class 4 claims in full approximately one year after confirmation, while repaying Brenholtz's claim over a much longer period (perhaps as long as 12½ years), constitutes unfair discrimination.[6] Cornwall could theoretically pay $2,870 per month to be distributed amongst all unsecured non-insider claimants, of which Brenholtz would receive 98%. As a result, at the end of one year, Brenholtz would receive approximately $33,750, as opposed to the $24,000 proposed by the Plan. The tradeoff, of course, is that Class 4 claims would be paid over many years.

There is support for the proposition that a plan which pays one class ahead of a similar dissenting class unfairly discriminates against such dissenting class. *See, e.g., In re Cranberry Hill Assocs. Ltd. P'ship*, 150 B.R. at 290-91 (finding unfair discrimination where one class would be paid upon effective date of plan while other class would be paid nine years into the future); *In re Baugh*, 73 B.R. 414, 417 (Bankr. E.D. Ark. 1987) (finding unfair discrimination where one class would be paid in full before other class of similar claims). However, other courts have found no unfair discrimination where similar classes are paid over a different period of time, so long as both classes are paid the same percentage, and so long as the increased delay and risk to the longer-payout class is addressed by paying such class appropriate interest. *See In re Crosscreek Apartments Ltd.*, 213 B.R. 521, 538 (Bankr. E.D. Tenn. 1997) (recognizing that two classes may "simply be paid the same amount . . . such that while the two classes will be paid at different times, the net amount realized will be the same (absent the risk inherent in any payment delay)"); *In re Sherwood Square Assocs.*, 107 B.R. 872, 880 (Bankr. D. Md. 1989)

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[6]There is some confusion as to how long it will take to pay off Class 4 claims. See *supra* note 2.

("The comparison is thus between payment in cash on the effective date and payment over time at 14½ percent annual interest. The Court concludes the different treatment at such a high rate of interest which compensates for risk is neither unfair discrimination nor inequitable"). Thus, where a plan proposes to pay similar classes over different periods of time, such classes must receive the same percentage, and the risk and delay associated with a lengthier payout must be minimized by the payment of interest. *See id.* The plan's feasibility, which factors into the risk equation, is also important. *See In re Sherwood Square Assocs.*, 107 B.R. at 880.

To resolve this issue, the court applies the four factors set forth above. Whether Cornwall satisfies the first two factors – reasonable basis for discriminating treatment and ability to carry out a plan – is questionable. It may be reasonable to pay a much larger, contested judgment creditor over a longer time frame. But, it is certainly possible to pay the Class 4 creditors over the same period of time. Cornwall's ability to make payments is not affected and the Plan is no less feasible if Class 4 and Brenholtz are both paid on a pro rata basis.

Of greater significance to the court, however, is whether the Plan's treatment of Brenholtz's claim is fair and proposed in good faith. The good faith element is discussed at paragraph C, *infra*.

Brenholtz's treatment, while discriminatory, is not unfair, and the discrimination is narrowly tailored. First, unlike Class 4, Brenholtz is to receive interest at 6 % until his claim is paid in full. Relative to Class 4, this interest compensates Brenholtz for the delay and risk associated with a lengthier payout.[7] The Plan provides for payment in full to both Class 4 and

[7]For purposes of the unfair discrimination analysis, the court considers the 6% rate as it relates to the treatment of Class 4, as unfair discrimination looks to the fairness of treatment between classes of similar priority. *See In re Sentry Operating Co. of Tex. Inc.*, 264 B.R. 850, 863 (Bankr. S.D. Tex. 2001). Whether the 6% interest

Brenholtz, thus there is equality of repayment. Brenholtz concedes that Cornwall's business is sound and that the Plan is feasible. Thus Brenholtz does not dispute Cornwall's ability to pay Brenholtz well into the future. Case law supports the conclusion that the disparate treatment between Class 4 and Brenholtz is not unfair. *See In re Crosscreek Apartments Ltd.*, 213 B.R. at 538; *In re Sherwood Square Assocs.*, 107 B.R. at 880.

Second, after Class 4 is paid off in one year, the $870 monthly payment earmarked for such class will thereafter be paid to Brenholtz, for a combined monthly payment of at least $2,870. Although Brenholtz will receive less under the Plan in the first year than he would were his claim and Class 4 paid out at the same time, he will receive more in subsequent years. Additionally, not only will Brenholtz receive the $870 to Class 4 once that class is retired, but he will receive increased monthly payments as other classes are paid off. Namely, he will receive an additional $1,000 per month as administrative claims are paid off after twenty months; an additional $2,233 per month as Class 2 is paid off after sixty months; and the amount paid to Class 1 once that class is retired, until the monthly payment to Brenholtz equals $6,000, at which time he will receive a maximum of $6,000 per month. Third, Brenholtz will immediately receive any funds realized from Cornwall's lawsuit against Travelers. No other class will receive any portion of any such recovery unless Brenholtz is paid in full.

The Plan effectively counterbalances any unfairness against Brenholtz by affording him some rights not allowed other classes: receipt of potential Traveler's lawsuit proceeds; interest accrual; and progressively increased payments on his claim as other classes are retired, as

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rate satisfies the fair and equitable requirement under section 1129(b)(2)(B)(i) is a different matter. *See* discussion *infra* Part II.D.

opposed to dividing such payments amongst all remaining classes of equal or greater priority. The Plan does not unfairly discriminate against Brenholtz. *See In re Crosscreek Apartments Ltd.*, 213 B.R. at 538; *In re Sherwood Square Assocs.*, 107 B.R. at 880.

C. Good Faith

Brenholtz contends that Cornwall has not proposed the Plan in good faith. While Brenholtz provides no specific arguments or examples of alleged bad faith, Brenholtz's objection suggests three such bases. First, Brenholtz argues that he does not receive fair treatment relative to similar claimants. *See* Objection of David Brenholtz to Debtor's First Amended Combined Plan and Disclosure Statement, ¶ 5. This argument has been considered within the context of classification and unfair discrimination. Second, Brenholtz argues that "the proposed plan is merely to provide a scheme to delay payment [to Brenholtz] . . . the bankruptcy was filed merely to avoid the necessity of filing a supersedeas bond in the underlying lawsuit which Debtor seeks to overturn the Judgment on appeal." *Id.* Third, Brenholtz argues that the Plan fails to commit the full range of Cornwall's available resources to pay debts. *See id.* ¶ 6.

The court may not confirm the Plan unless the Plan "has been proposed in good faith." 11 U.S.C. § 1129(a)(3) (2002). Whether a plan has been proposed in good faith turns on the totality of the circumstances surrounding the plan and the bankruptcy filing. *See, e.g., Noreen v. Slattengren*, 974 F.2d 75, 76 (8th Cir. 1992). The court's decision on good faith is a question of fact. *See Humble Place Joint Venture v. Fory (In re Humble Place Joint Venture)*, 936 F.2d 814, 816 (5th Cir. 1991).

"In essence, the good faith inquiry looks at the debtor's fairness in dealing with creditors." *Barger v. Hayes County Non-stock Co-op (In re Barger)*, 233 B.R. 80, 84 (B.A.P. 8th

Cir. 1999). The Fifth Circuit has held that, "[w]here the plan is proposed with the legitimate and honest purpose to reorganize and has a reasonable hope of success, the good faith requirement . . . is satisfied." *Heartland Fed. Sav. & Loan Ass'n v. Briscoe Enters. Ltd. (In the Matter of Briscoe Enters. Ltd.)*, 994 F.2d 1160, 1167 (5th Cir. 1993), *quoting Brite v. Sun Country Dev. Inc. (In the Matter of Sun Country Dev. Inc.)*, 764 F.2d 406, 408 (5th Cir. 1985). Also of importance is whether the debtor or its principals will retain any equity interests. *See In the Matter of Briscoe Enters. Ltd.*, 994 F.2d at 1167. Thus, the primary factors to consider in determining whether a plan has been proposed in good faith are: (1) whether the plan is proposed with the legitimate and honest purpose to reorganize; (2) whether the plan has a reasonable hope of success; and (3) whether debtor or its principals will retain any equity interests. *See id.*

Several courts have applied an almost per se rule that filing for bankruptcy in lieu of posting a supersedeas bond is bad faith. *See In re Karum Group Inc.*, 66 B.R. 436, 438 (Bankr. W.D. Wa. 1986); *In re Smith*, 58 B.R. 448, 449-50 (Bankr. W.D. Ky. 1986); *In re Wally Findlay Galleries (New York) Inc.*, 36 B.R. 849, 850 (Bankr. S.D.N.Y. 1984). In the Fifth Circuit, however, as in the majority of courts, filing for bankruptcy in lieu of posting a supersedeas bond is not the determinative issue when examining the debtor's good faith. *See Little Creek Dev. Co. v. Commonwealth Mortgage Corp. (In the Matter of Little Creek Dev. Co.)*, 779 F.2d 1068, 1071-72 (5th Cir. 1986) ("When compared with the several general indicia of bad faith previously discussed [the fact that bankruptcy was filed solely to avoid the requirement of a supersedeas bond does] not rise to the level of egregiousness necessary to conclude that the reorganization process is being perverted"); *In re McLaury*, 25 B.R. 30 (Bankr. N.D. Tex. 1982).

See also In re Muskogee Envtl. Conserv. Co., 236 B.R. 57, 67-68 (Bankr. N.D. Okla. 1999); *In re Fox*, 232 B.R. 229, 234 (Bankr. D. Kan. 1999); *In re Boynton*, 184 B.R. 580, 583 (Bankr. S.D. Cal. 1995); *In re Corey*, 46 B.R. 31, 33 (Bankr. D. Haw. 1984). Thus, even if Cornwall filed its petition solely to avoid the necessity of posting a supersedeas bond, the court should not consider this as conclusive of the good faith issue, but should instead consider this possibility as one factor among many that aides the court in its totality of the circumstances inquiry. *See id. See also In re Fox*, 232 B.R. at 234.

In addition, many courts that have examined this issue hold that the real inquiry into whether the failure to post a supersedeas bond constitutes bad faith "should be on whether the debtor had the ability to post the bond without losing the ability to stay in business." *In re Fox*, 232 BR at 234; *Accord Marsch v. Marsch (In re Marsch)*, 36 F.3d 825, 829 (9th Cir. 1994); *In re Boynton*, 184 B.R. 580, 582 (Bankr. S.D. Cal. 1995). These cases rely on the frequently cited case of *Alton Telegraph* for the proposition that a debtor may file a Chapter 11 case to avoid posting a supersedeas bond when the debtor is protecting a legitimate and ongoing business concern. *In re Alton Tel. Printing Co.*, 14 B.R. 238, 240-41 (Bankr. S.D. Ill. 1981). *See also Dowd & Dowd v. Gleason (In re Gleason)*, 2001 WL 1597960 (Bankr. N.D. Ill. 2001); *In re Sletteland*, 260 B.R. 657, 664 (Bankr. S.D.N.Y. 2001).

It is clear that Cornwall would not have filed for bankruptcy had Brenholtz not obtained his judgment, and had Cornwall had the ability to post a supersedeas bond. However, with the referenced case law as a backdrop, the mere fact that the Brenholtz judgment prompted Cornwall's filing is not dispositive of the issue. Indeed, many debtors routinely file for bankruptcy protection to avoid collection or foreclosure. There is nothing inappropriate with

such filings, so long as the debtor honestly, legitimately, and realistically seeks to reorganize. *See In the Matter of Little Creek Dev. Co.*, 779 F.2d at 1071-72.

In the present case, Cornwall lacked the ability to post a supersedeas bond. Cornwall had an ongoing and otherwise profitable business concern to protect. Most importantly, Cornwall has not used the Code to pass time pending the outcome of its appeal. Cornwall filed this case on April 12, 2002. The hearing on confirmation of the Plan was held on December 19, 2002. Cornwall has moved its case efficiently and rapidly through bankruptcy. Perhaps, had Cornwall lingered and not proceeded forward with its case, a finding that Cornwall has misused bankruptcy as a replacement for a supersedeas bond would be easier. Cornwall, however, has recognized that it has a large liability to Brenholtz, and, while attempting to defeat that liability in state court, nevertheless realizes that it *is* currently liable, and it is attempting to salvage its business operations while at the same to paying its creditors 100 %. Brenholtz has introduced no evidence of bad faith, except his vague contention that the bankruptcy is a mere substitute for a supersedeas bond. Cornwall has proven, however, that it is not employing bankruptcy as such a substitute, but is instead attempting an honest and legitimate reorganization.

With respect to Brenholtz's argument that Cornwall fails to commit the full range of its available resources to pay its creditors, Brenholtz cites to no law to support his argument that this is a requirement for confirmation of a Chapter 11 plan, nor is any such law readily apparent from a quick review of the Code and the available case law. *Compare* 11 U.S.C. 1129 (2002) (providing no requirement that all surplus income or resources be used to fund plan), *with* 11 U.S.C. 1325(b)(1)(B) (2002) (mandating that Chapter 13 plan must commit all of the debtor's disposable income to plan in order to confirm plan over objections). In fact, the law suggests

that Chapter 11 contains no requirement that a debtor must commit *all* of its resources, profit, or surplus cash flow to fund its plan, *see, e.g., In re Keenan*, 195 B.R. 236, 243 (Bankr. W.D.N.Y. 1996) ("there is no requirement of law that the debtors commit, on an ongoing basis, any portion of their post-petition personal service income to their creditors or to a Plan of Reorganization"), although some courts admittedly consider the amount committed by an *individual* Chapter 11 debtor into funding his plan in the good faith analysis, *see, e.g., In re Kemp*, 134 B.R. 413, 415 (Bankr. E.D. Cal. 1991).

Based on the evidence presented, the court cannot conclude that Cornwall will have significant resources over and above those which Cornwall commits to funding its Plan. The court is satisfied that Cornwall is sufficiently funding its plan.

Finally, the evidence demonstrates that Cornwall's business is sound and that it has a bright future given Cornwall's unique position in the local insurance industry and recent trends among insurers in the State of Texas. Thus, Cornwall's Plan is feasible – a point conceded by Brenholtz. Cornwall has proposed the Plan in good faith within the meaning of section 1129(a)(3). *See Heartland Fed. Sav. & Loan Ass'n v. Briscoe Enters. Ltd. (In the Matter of Briscoe Enters. Ltd.)*, 994 F.2d 1160, 1167 (5th Cir. 1993).

D. Fair and Equitable Standard under § 1129(b)

Section 1129(b) has two components: the plan must not unfairly discriminate against the dissenting, impaired class, and the plan's treatment of such class must be fair and equitable. 11 U.S.C. § 1129(b)(1). In the instant case, the parties presented very little argument regarding the fair and equitable test. In fact, it may be implied that this is not a point of dispute between the parties. Nevertheless, the court has an independent duty to insure that a plan satisfies *all*

confirmation requirements, even in the absence of a specific objection. *See, e.g., In the Matter of Chaffin*, 836 F.2d 215, 216 (5th Cir. 1988).

Section 1129(b)(2)(B)(i) provides that the fair and equitable condition is satisfied as to an unsecured class if "each holder of such class receive or retain on account of such claim property of a value, as of the effective date of the plan, equal to the allowed amount of such claim . . . ." 11 U.S.C. § 1129(b)(2)(B)(i). The court must be satisfied, therefore, that Brenholtz is receiving the present value of his claim. Does the proposed stream of payments and the 6% interest rate provide Brenholtz with the present value of his claim? The analysis here is very brief as no relevant evidence was submitted on this issue. Cornwall offered evidence of the federal judgment rate of 1.47% and contends that, since the proposed rate of 6% is much greater, the treatment of Brenholtz's claim is more than fair. The court notes that the rate on the judgment itself is 10%. Evidence of judgment rates does not provide the court with any guidance on the question of whether Brenholtz is receiving the present value of his claim. In short, the court is not persuaded that the Debtor has met its burden on this point. The court cannot, therefore, find that Cornwall has satisfied the requirements of section 1129(b) of the Code.

E. Motion to Assume Lease

Brenholtz objects to Cornwall's motion to assume its unexpired commercial lease of the premises from which Cornwall maintains and operates its business. Brenholtz objects on the grounds that assumption of this lease "is not in the best interest of the corporation nor creditors of the corporation." Objection by David Brenholtz to Debtor's First Amended Combined Plan and Disclosure Statement ¶ 4. Brenholtz argues that Cornwall pays more for the lease than it needs to in order to carry on its business, and that other equally suitable property is available for

considerably less. Additionally, Brenholtz notes that Cornwall leases its premises from Ron Hettler – Cornwall's sole shareholder – and argues that such insider arrangement is ripe with possibilities for misuse and overcharging. Cornwall responds by noting that the location of its particular business is important to its success, because Cornwall is located close to its clientele in a newer, more affluent part of town, and that such clientele would be less willing to travel to a different part of town. Cornwall adds that the rent it pays for its premises is comparable to similar rates in the neighborhood, and that it pays fair market value for its premises.

The debtor's decision on assuming a commercial lease is entitled to deference under the business judgment test. *See Orion Pictures Corp. v. Showtime Networks Inc. (In re Orion Pictures Corp.)*, 4 F.3d 1095, 1099 (2d Cir. 1993); *In re Central Jersey Airport Servs. LLC*, 282 B.R. 176, 183 (Bankr. D.N.J. 2002); *In re ANC Rental Corp. Inc.*, 278 B.R. 714, 723 (Bankr. D. Del. 2002). "The best business judgment test generally requires a showing that assumption of an executory contract benefits and is in the best interests of the bankruptcy estate, and is the result of the exercise of reasonable business judgment." *In the Matter of GP Express Airlines Inc.*, 200 B.R. 222, 230 (Bankr. D. Neb. 1996). *Accord In re The Beare Co.*, 177 B.R. 879, 882 (Bankr. W.D. Tenn. 1994). "This determination must include a consideration of the effects that assumption would have on the debtor; the implications for the lessor; the benefit or detriment to unsecured creditors; and the significance of the lease to the debtor's reorganization." *In re Valley View Shopping Ctr. LP*, 260 B.R. 10, 39 (Bankr. D. Kan. 2001). *Accord In re Gateway Apparel Inc.*, 210 B.R. 567, 570 (Bankr. E.D. Mo. 1997). Of additional importance is the debtor's ability to perform under the lease. *See In re Washington Capital Aviation & Leasing*, 156 B.R. 167, 172-73 (Bankr. E.D. Va. 1993). Absent a showing of bad faith or abuse of the

debtor's discretion, the debtor's exercise of business judgment in deciding to assume an unexpired lease will generally not be disturbed. *See In the Matter of GP Express Airlines Inc.*, 200 B.R. at 230; *In re G Survivor Corp.*, 171 B.R. 755, 757 (Bankr. S.D.N.Y. 1994).

While the fact that the lessor is an insider of the debtor may give rise to somewhat heightened scrutiny, the law does not appear to alter the normal application of the business judgment rule:

> '[S]trict scrutiny' is not supported by the case law. Indeed, even the case cited . . . simply states that transactions involving insiders are necessarily subjected to heightened scrutiny because they are rife with the possibility of abuse. Moreover, [such case] involved the sale of the debtor's assets to a fiduciary pursuant to section 363, not the assumption of the unexpired leases under section 365. Thus, it is not even clear that the law requires heightened scrutiny, although it was prudent of the Bankruptcy Court to look closely at the assumption.

Westship Inc. v. Trident Shipworks Inc., 247 B.R. 856, 865 (M.D. Fla. 2000) (internal citations and quotations omitted). *Accord In re Trans World Airlines Inc.*, 261 B.R. 103, 122 (Bankr. D. Del. 2001) (noting that business judgment rule is appropriate in section 365 assumption of lease, and that nothing in the law mandates strict scrutiny of proposed assumption involving an insider).

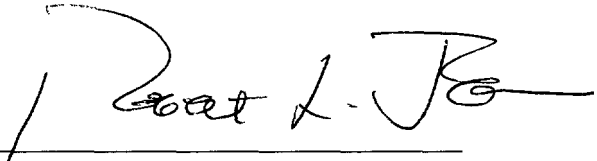
As conceded by Brenholtz, Cornwall's business is doing well. The location of his business cannot be discounted as a factor in its success. Under the circumstances, the court is not inclined to question Cornwall's judgment regarding assumption of the lease.

III. Conclusion

The court denies confirmation. The motion to assume lease is approved. Cornwall has 20 days from entry of the order denying confirmation to file a modification to the Plan addressing the Plan's single deficiency. Assuming Cornwall files a modified plan, a hearing on the modified plan will be set on the court's regular calendar and will be handled in accordance with section 1127 of the Code and Rule 3019 of the Federal Rules of Bankruptcy Procedure.

The court requests that Cornwall's counsel submit appropriate orders regarding plan confirmation and the motion to assume lease.

Signed February 28, 2003.



ROBERT L. JONES
UNITED STATES BANKRUPTCY JUDGE